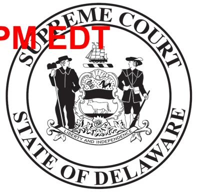
EFiled: May 07 2024 04:34PM EDT
Filing ID 72906360
Case Number 117,2024



IN THE SUPREME COURT OF THE STATE OF DELAWARE

RMP SELLER HOLDINGS, LLC, f/k/a NEW SAVE MART CORP., Respondent/Counterclaim-Petitioner Below, Appellant. v. SM BUYER LLC and SM TOPCO LLC, Petitioners-/Counterclaim-Respondents Below, Appellees.	))))))))))))	Court Below: Court of Chancery of the State of Delaware, C.A. No. 2023-0957-JTL

APPELLANT'S OPENING BRIEF

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Dated: May 7, 2024

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NATURE OF PROCEEDINGS

This appeal arises from a staggering arbitration award that inverted the understood economics of the parties' deal—forcing the seller to *pay* for the business it sold—by disregarding express agreement terms intended to avoid such an absurd result. It is an ideal vehicle to clarify precedent and confirm that radical awards issued with disregard for contractual terms remain subject to meaningful judicial review and may be vacated. The underlying award, and the Court of Chancery's order "reluctantly" confirming it, demonstrate the need to ensure that courts do not merely rubber stamp (and thereby encourage more) cynical post-closing gambits like those that led to the award here. The Court should therefore take this opportunity to provide parties needed certainty in their deal-making and trial courts with further guidance on when they can reject arbitration awards for manifest disregard of the law.

RMP Seller, LLC ("Seller") sold Save Mart, a regional supermarket operation, along with Save Mart's joint venture interest in a processing and distribution business (Super Store Industries, Inc. ("SSI")), to a private-equity firm, SM Buyer, LLC ("Buyer"), for $245 million. As a part of that transaction, at Buyer's request, Seller's interest in SSI was spun out and sold separately for the specified, "aggregate" price of $90 million (which was deducted from the $245 million).

Buyer was aware that SSI carried $109 million in debt (the "SSI Debt"), and Seller's pro rata share of that debt was baked into the aggregate price.

At Closing, Buyer promulgated a Pre-Closing Statement that did *not* classify the known SSI Debt as "Indebtedness"—which would have required an adjustment to the overall Purchase Price—because the pro rata share of the SSI Debt was already included in the aggregate $90 million SSI Purchase Price. As a result, at Closing, Buyer contributed funds, debts were paid off, and Seller received net proceeds of $32.6 million along with a Buyer-funded $7 million purchase price adjustment escrow. Ninety days later, exercising its authority to adjust the Closing Statement under section 1.4(d) of the equity purchase agreement ("EPA"), Buyer returned adjustments. These included a staggering increase of Indebtedness from $29 million to $138 million, calculated by adding the $109 million of SSI Debt. Buyer took this brazen position even though the SSI Debt had never been treated as a Save Mart liability on its audited financial statements, was not paid off at Closing, was not in default, and was secured by ample SSI assets in the form of inventory and accounts receivable (not to mention extremely valuable land).

Seller disputed this massive adjustment, and the parties agreed to arbitrate this issue while sending other disputes involving more conventional adjustments to an accounting referee. During the arbitration, Seller discovered evidence that Buyer never included the SSI Debt as a recoverable item in its own internal analyses

leading up to Closing, and Buyer's own accountants advised before Closing that SSI Debt was not includable in Indebtedness because it was "outside the consolidation perimeter." In other words, as the Court of Chancery noted, Save Mart's audited financials never treated the SSI Debt as debt of Save Mart. Buyer's witnesses even testified they: (a) were aware that Seller did not consider SSI Debt to be includable in Indebtedness that would be subtracted from the Purchase Price; yet (b) made the "strategic" decision to remain silent about their intention to raise it until after Closing.

The Accounting Rules in the parties' EPA foreclosed Buyer's reclassification of the debt because Buyer's position both required double counting the debt and was inconsistent with historical accounting practices. But instead of applying the Accounting Rules, the Arbitrator concluded they did not constrain Buyer's adjustments to Indebtedness *at all*. After sweeping aside these crucial guardrails, the Arbitrator determined the EPA's definition of Indebtedness, in isolation, could be read to include SSI Debt, and therefore the debt adjustment was allowable. He awarded Buyer a post-closing adjustment of $87,427,170.51, plus interest, which effectively converted the $90-million sale to a $20 million payment *by Seller* for the privilege of conveying its valuable SSI interest.

The Court of Chancery was understandably flabbergasted by that outcome. It explained that the Award "radically changed the economics" of the transaction,

"made no sense," and generated an outcome that was "so economically divorced from the intended transactions as to be comparable to" the post-closing adjustment this Court addressed in *Chicago Bridge & Iron Co. N.V. v. Westinghouse Elec. Co. LLC*. Even though it recognized the Award was wrong, and said it would have ruled differently, the court nevertheless confirmed the Award on the belief the applicable standard of review compelled that unjust result.

But the law does not handcuff courts or insulate all arbitration awards from meaningful judicial review. This Court has made clear that awards should be vacated when they are based on a manifest disregard of the law. Critically, a disregard of the law includes disregard for the terms of a contract. Here, the arbitrator issued an award that inverted the parties' deal by disregarding the EPA's express mandate to apply the EPA's stated Accounting Rules as constraints on the Post-Closing Statement. By reading those express constraints out of the EPA, the Award reclassified a material liability (SSI Debt) in a way that double counted that debt and was directly at odds with Seller's known, historical treatment of it.

The Award could only have resulted, and in fact did result, from a manifest disregard of the law. Courts have consistently refused to allow buyers to apply new accounting rules post-closing, especially where they seek thereby to recover material, known debts they declined to raise pre-closing and are foreclosed from collecting by the terms of the deal. And the cases establish that an arbitration award

that ignores such contractual terms, and thereby fundamentally changes a deal, is properly vacated.

The Court should confirm and clarify that precedent here. The Arbitrator manifestly disregarded both Delaware law and the express provisions of the EPA by refusing to give effect to the agreed-upon Accounting Rules that impose clear and important constraints on what can be counted as Indebtedness. The Court of Chancery recognized the Award was obviously wrong, but it, too, overlooked that the Award wrote the Accounting Rules out of the agreement. This Court should reverse the order confirming the Award (and order that the Award be vacated instead) because the Arbitrator refused to apply the Accounting Rules stated in the parties' EPA as constraints on Buyer's gambit to demand a post-Closing adjustment for long-term debt that Buyer had always been aware of and that had already been baked into the purchase price.

SUMMARY OF THE ARGUMENT

The Court should take this opportunity to clarify that, on appropriate judicial review, arbitration awards that rewrite a transaction and invert its economics by ignoring express terms are properly vacated.

1. The Court of Chancery erred by declining to vacate the Award after concluding that it blessed a post-Closing adjustment that violated the plain terms of the EPA and radically upended the parties' intent and the deal's economics. The Accounting Rules set out in the EPA were expressly and repeatedly specified as the key constraint on the post-Closing adjustment process. In the Award, the Arbitrator construed section 1.4(d) of the EPA, and specifically the phrase "as applicable," as license to disregard the Accounting Rules for all adjustable components of the Purchase Price (except Working Capital). Section 1.4(d) cannot reasonably or rationally be interpreted in this way, and the Accounting Rules expressly precluded reclassifying SSI Debt as Indebtedness or double counting SSI Debt.

2. The Arbitrator relied upon extrinsic evidence supporting Buyer's interpretation while excluding other extrinsic evidence favoring Seller's interpretation. No reasonable arbitrator could admit only extrinsic evidence that supported one interpretation, while barring consideration of damning evidence demonstrating that interpretation was faulty and another interpretation correctly comported with the parties' contemporaneous understanding and intent.

3. The post-Closing adjustment process is meant to capture changes in finances during the short period between signing and closing. It is not an opportunity for a buyer to lie in wait and surprise a seller with a radical reclassification of debt that both parties long knew about and thereby effect a $109 million swing in the transaction—one that forced the seller effectively to buy what it thought it had sold.

4. Though the Court of Chancery recognized the Award made no sense under the terms of the deal, and subverted the deal's obvious intended economics, it misapplied *SPX Corp. v. Garda USA, Inc.*, 94 A.3d 745, 750 (Del. 2014), in declining to vacate the Award. In *SPX*, the disputed contract term was subject to two plausible interpretations, and therefore this Court held the trial court should not have disturbed the arbitrator's determination. Here, by contrast, there was only *one* plausible interpretation that fit the text of the EPA and the parties' intent: the Accounting Rules are an express constraint on all adjustable components of the Purchase Price and must be enforced, not casually disregarded. An arbitrator is not interpreting an agreement if his award removes express, critical, and commonplace protections for sellers in material transactions. By focusing on the Arbitrator's analysis of the isolated definition of Indebtedness, the Court of Chancery failed to recognize the Arbitrator disregarded the Accounting Rules, and disregarding the terms of a contract is a proper basis for vacating an award.

BACKGROUND

A. RELEVANT FACTS

1. The Parties

Seller is a California limited liability company that, prior to Closing, owned all the equity interests of Save Mart. Save Mart is a California limited liability company and a three-generation, family-owned operator of about 200 grocery stores throughout California and Northern Nevada under the banners of Save Mart, Lucky California, and FoodMaxx. A1196. Save Mart also owned a slight majority joint venture interest in a different entity, Super Store Industries ("SSI"). A1204-A1205. Prior to Closing, at Buyer's request, that interest was transferred to the newly-formed SSI Holdco, in which Seller also owned all the equity interest. A432-A433.

Buyer is a Delaware limited liability company formed by private equity firm Kingswood Capital Management, LP ("Kingswood") for its acquisition of Save Mart and the SSI interest. A371, A1196-A1197. Topco is a Delaware limited liability company and affiliate of Buyer. A502. In a pre-Closing Amendment to the EPA, Buyer designated Topco (instead of Buyer) to separately acquire the SSI interest. A502-A505.

Pursuant to the EPA and Amendment, Seller sold its equity interests in Save Mart to Buyer and its equity interests in SSI Holdco to Topco. A372-A373, A502-A504.

2. <u>The SSI Partnership & SSI Debt</u>

In 1992, three local grocers, including Save Mart, formed SSI, a California general partnership, to engage in the wholesale distribution of food products to grocery stores. A1544, A1560. Though Save Mart was a general partner of SSI, on any theoretical default of SSI's debt, the partnership agreement provided that Save Mart would be entitled to indemnification from SSI to the extent of any SSI assets. A1558 (partners entitled to reimbursement "for any and all direct costs and expenses of the Partnership paid or incurred by such Partner").

Save Mart's auditors never identified material risk to Save Mart from SSI Debt, repeatedly confirming its practice of carrying the SSI investment at its net equity, book value (including *pro rata* share of SSI Debt). A555, A569, A586, A600-A601 (each showing Save Mart's 2018-2020 audited financial statements, which classified the SSI interest, inclusive of debt, as a Save Mart asset); Ex. A, 4-5 ("Seller historically carried the [SSI] interest as an equity investment … including a proportionate allocation of the [SSI Debt]."). SSI has always serviced SSI Debt without contribution from any general partner. A857-A858, A2191, A2322. Save Mart has never been asked to make good on any portion of SSI Debt, and SSI Debt has never been in default. A857-A858, A2191, A2322.

At Closing, SSI carried debt of approximately $109 million, comprising an asset-backed revolving line of credit used to finance inventory purchases (about $75

million) and a term loan used to fund bottling equipment improvements (about $33 million). A1302, A1425-A1695 (SSI loan agreements). Buyer was fully aware of this debt prior to the March 2022 closing. A1168 (9/27/21 Kingswood bid analysis referencing "$34mn real estate debt" and "$70mn of revolving debt").

3. Initial Due Diligence and the LOI

Kingswood's initial bid analysis from September 2021 also shows that it did not regard SSI Debt as a material risk. A1204 (noting that revolving line was amply covered by SSI accounts receivable and inventory). During due diligence, Kingswood received copies of Save Mart's audited financial statements for the year ending December 27, 2020. A1250-A1281, A2315-A2316.[1] With respect to its SSI interest, Save Mart's audited financial statements classified the SSI interest as a single net asset line item, "Investment in Joint Venture." A1255, A1260, A1269-A1270. The SSI interest was carried at approximately $22 million net equity. A1255. Note 6 to the audited financial statements confirms the SSI interest was valued net of a *pro rata* share of SSI Debt. A1269-A1270.

On December 23, 2021, Kingswood issued a letter of intent, countersigned by Save Mart, providing that Kingswood would pay $270 million[2] for Save Mart, including its SSI interest, subject to adjustments for Working Capital, Closing Cash,

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[1] As noted below, these audited financial statements were later attached to the EPA and formed part of the definition of Accounting Rules. A383-A384.

[2] Prior to Closing, the parties agreed to reduce this amount to $245 million. A2196.

Closing Date Indebtedness, and Transaction Expense. A512-A523. The LOI expressly stated that Kingswood would agree to a definition of Indebtedness (with a capital "I") consistent with debt-like items identified on Appendix B thereto. A516. Although Appendix B does list Save Mart's own operating line of credit as debt, it does not include the distinct SSI Debt. A522, A2319-A2320.

4. <u>Kingswood's Internal Analysis of the Transaction</u>

Throughout the deal, Kingswood updated its initial bid analysis, once in a "Co Investment Information Memorandum" in January 2022 before Closing (A1756-A1773) and again after Closing in an "Investor Committee Memorandum" dated April 2022 (A1193-A1246). In these analyses, Kingswood forecasted low, mid, and high valuations for SSI's two key real property assets, Lathrop and Turlock. A1204-A1205, A1765. The total value estimates for SSI ranged from $170 to $200 million. A1168-A1169, A1204-A1205, A1290. Estimates of Save Mart's proportional interest in SSI were between $90 and $100 million. A1168-A1169, A1204-A1205, A1290.

Each analysis also identifies SSI Debt (including component parts). A1168-A1169, A1204-A1205, A1290. Kingswood noted the term loan would be a deduction at sale of the Lathrop property (if not paid off earlier). Kingswood also repeatedly noted that SSI's inventory and accounts receivable—the fruits of the asset-backed portion of SSI Debt—were more than sufficient to cover the debt from

the revolving line of credit. A1168-A1169, A1204-A1205, A1290. None of these analyses identified SSI Debt as a material risk. A1168-A1169, A1204-A1205, A1290.

On February 2, 2022, at Kingswood's request after execution of the LOI, Seller delivered copies of the SSI loan agreements. A1425-A1695. Later that same day, Kingswood delivered a revised draft of the EPA. A1303-A1415. In this draft, Kingswood proposed to amend section 6.14 (Reorganizations) to provide for the separate sale of the SSI Interest as follows:

> (b) Company shall distribute its interest in Super Store Industries, a California general partnership (the "SSI Interest") to Seller, Seller shall subsequently contribute the SSI Interest to a newly-formed limited liability company owned by Seller ("SSI Holdco") and the Parties shall amend this Agreement to incorporate customary terms providing for (A) the purchase by Buyer or an Affiliate thereof of all of the limited liability company interests of SSI Holdco from Seller at the Closing for [______] (the "SSI Purchase Price") and (B) the Purchase Price to be decreased by the SSI Purchase Price … .

A1370. Thus, Buyer's amendment provided the SSI interest would be distributed out of Save Mart before Closing to SSI Holdco and sold separately to Buyer or its designee (to be specified by further pre-Closing Amendment). A1370. Kingswood also proposed the SSI interest would be sold for a specific "SSI Purchase Price," which would be a reduction to the Purchase Price it would otherwise have paid for Save Mart (since Save Mart would no longer own the SSI interest). A1370.

On January 17, 2022, Kingswood had identified for its accountant, Grant Thornton, the "net valuation" of the SSI interest at $90 to $101 million. A1757, A1765 (directing Grant Thornton to "See page 8 for SSI valuation," which specified a "net value" of the SSI interest at $90 to $101 million). On February 8, 2022, after Kingswood proposed its "sold separately" amendment, Grant Thornton circulated a "proposed allocation methodology for SSI," containing a spreadsheet starting with Kingswood's $90 million net valuation and including a proportional share of SSI Debt. A1299-A1301 (email), A1302 (PP Allocation worksheet, cells D5 and D6). The Parties thereafter revised section 6.14 of the EPA to assign a fixed, *net positive* SSI Purchase Price of the same $90 million. A432-A433.

The EPA was executed on March 7, 2022. A371. On March 25, 2022, the eve of Closing, the parties executed the Amendment, repeating the $90 million SSI Purchase Price and describing it as the "aggregate" price for the SSI interest. A502. In short, the $90 million SSI Purchase Price is not an arbitrary figure—it is the net, fixed, aggregate value that was to be paid to Seller for the SSI interest. A371, A502.

5. <u>Revisions to the Disclosure Schedule to Call out SSI Debt</u>

On February 6, 2022, by way of response to Kingswood's proposed revision to section 6.14 described above, Seller returned a revision to section 3.6 of the Disclosure Schedule to call out the two components of SSI Debt. A1799. At Buyer's

prior request, in the corresponding section 3.6 of the EPA, the purchase price components had been expressly linked to the Disclosure Schedule as follows:

> 3.6 Undisclosed Liabilities. **Except as set forth on Section 3.6 of the Company Disclosure Schedule, neither the Company nor any of the Operating Subsidiaries have any material Liabilities, other than** (a) as disclosed in, set forth on, or reflected and adequately reserved against in the Balance Sheet, (b) those incurred in the Ordinary Course of Business since the Balance Sheet Date …, and **(c) those Transaction Expenses, Indebtedness, Working Capital and unpaid credit card processor's fees, costs and expense items fully included in the calculation of the Closing Payments.** Except as set forth on Section 3.6(b) of the Company Disclosure Schedule and except for the Transaction Expenses, the Company has no liabilities in respect of [certain fees and commitments].

A384 (emphasis added).

Thus, any liabilities of Save Mart or its Operating Subsidiaries (defined to include SSI) must *either* (a) be included in the liability categories of the purchase price (such as Indebtedness) *or* (b) be scheduled in section 3.6 of the Disclosure Schedule. Liabilities cannot appear *both* in section 3.6 of the Disclosure Schedule and, for instance, as Indebtedness, as these are express *alternative classifications*. A384. By scheduling SSI Debt in section 3.6, the parties confirmed their understanding that SSI Debt was distinct from, and would not be counted as part of, Closing Date Indebtedness. A384. Buyer accepted this revision. A646.

6. Testimony of Grant Thornton Accountant Regarding SSI Debt

Gokhan Tumel of Grant Thornton worked on this transaction for Kingswood. A915. Tumel's stated expertise was in reviewing sale agreements with a focus on

assessing debt. A2215-A2216. On January 14, 2022, after receiving a draft of the EPA (A1888), Tumel delivered his spreadsheet analysis, wherein his team expressly stated that SSI Debt was "not included as part of Indebtedness." A1755 (DDL Worksheet, Column G, Other Considerations Item and Note 1 ("**SSI reported debt** represents the proportional net debt of the SSI JV. *These liabilities are not included as part of Indebtedness* as the JV balance sheet is outside the consolidation perimeter.") (italics added)). Kingswood did not object to this analysis; instead, Kingswood promptly circulated this analysis to its investors—conveying Tumel's conclusion without caveat. A2113-A2134 (circulating A1755 at 4:37 p.m.).

In short, Kingswood's accounting experts at Grant Thornton, with a draft EPA in hand, determined that SSI Debt would not be included within "Indebtedness" because Save Mart's financial statements did not treat it that way. A1755.

7. <u>The Transaction</u>

As Buyer had requested, the EPA, signed March 7, 2022, provided in section 6.14(b) for the separate sale of the SSI interest, including an undivided interest in all balance sheet items therein, to Buyer or its designee for the agreed price of $90 million. A432-A433. As contemplated by section 6.14, prior to Closing, the Parties amended the EPA on March 25, 2022, to restate sections 1.1 to 1.3 entirely. A502-A503. Section 1.1, as amended and restated, specified that the SSI interest would be sold, not to Buyer, but rather to Buyer-affiliate Topco. A502. In service of this

sold-separately provision, prior to Closing, Seller caused the SSI general partnership interest (inclusive of its debt) to be distributed from the Save Mart operating company to Seller and, in turn, to SSI Holdco. A1079-A1084. And, at Closing, the SSI Holdco member interests were sold to Topco. A502-A503.

Also as required by section 6.14, section 1.2 of the EPA was amended and restated to specify (in pertinent part) that the aggregate SSI Purchase Price of $90 million was to be treated as a reduction to the Purchase Price for Save Mart:

> 1.2 Determination of Estimated Purchase Price. The aggregate consideration payable by Buyer in respect of the Company Membership Interests shall be an amount equal to (a) the Base Value, … minus (e) Closing Date Indebtedness, … **minus (h) the SSI Purchase Price (such resulting amount … the "Purchase Price"), and the aggregate consideration payable by Topco in respect of the SSI Holdco Membership Interests shall be an amount equal to $90,000,000** ("SSI Purchase Price").

A502 (emphasis added). In this language, the SSI Purchase Price is described even more specifically now as the "**aggregate consideration** payable by Topco" for the SSI interest. A502. Thus, the SSI basket of assets and liabilities was set apart in SSI Holdco and sold for the aggregate, fixed price of $90 million.

8. Determination of the Purchase Price

Section 1.4 of the EPA (Adjustment of the Estimated Purchase Price) imposes guardrails on the estimation and adjustment of the purchase price. A373-A377.

Sections 1.4(a) and (d) provide that the Pre-Closing Statement and Closing Statement must be prepared in a "manner consistent with" the Definitions *and the*

specified Accounting Rules. A373-A374. Crucially for this case, Buyer's right to adjust the Closing Statement is specified in section 1.4(d):

> 1.4(d) Closing Statement. No later than ninety (90) days after the Closing Date, Buyer shall cause to be prepared in good faith and delivered to Seller a statement (the "Closing Statement") setting forth Buyer's calculation of the Purchase Price (the "Closing Date Purchase Price"). The Closing Statement shall be prepared in a manner consistent with the definitions of the terms Working Capital, Closing Cash, Closing Date Indebtedness, Transaction Expenses, including, as applicable, the Accounting Rules (including as reflected on Exhibit A). The Parties agree that the purpose of preparing the Closing Statement and determining the Working Capital, Closing Cash, Closing Date Indebtedness, and Transaction Expenses is to measure the amount of the Working Capital, Closing Cash, Closing Date Indebtedness, and Transaction Expenses and such processes are not intended to (x) permit the introduction of accounting methods, policies, principles, practices, procedures, classifications or estimation methodologies for the purpose of determining the Working Capital, Closing Cash, Closing Date Indebtedness, or Transaction Expenses that are different than the Accounting Rules or (y) adjust for errors or omissions that may be found with respect to the Company Financial Statements or any inconsistencies between the Company Financial Statements and GAAP (except to the extent resulting from the application of the Accounting Rules in accordance with this Agreement).

A374. Section 1.4(d) references the Accounting Rules *twice*, specifying the process is not to permit "accounting methods" or "classifications … that are different from the Accounting Rules." A374.

The Accounting Rules are then defined in section 11.1 of the EPA as follows:

> "Accounting Rules" means, collectively, (i) the rules, methods, and principles set forth on Exhibit A (collectively, the "Agreed Principles"), (ii) the accounting principles, methods and practices used in preparing the audited Company Financial Statements dated December 27, 2020 (collectively, the "Historical Principles") and (iii) GAAP; provided,

> that in the event of any conflict among the Agreed Principles, the Historical Principles and GAAP, then the Agreed Principles shall take precedence, followed by the Historical Principles, followed by GAAP.

A450.

Two Accounting Rules are particularly relevant here. First, Agreed Principle 3 precludes double counting "of any item to be included in the Statements." A472. Because, as the Court of Chancery noted, the net asset value already included a proportionate share of SSI Debt (Ex. A, 4-5), SSI Debt could not be included as Indebtedness without violating this double counting prohibition.

The second element of the Accounting Rules, Historical Principles, also preclude reclassifying SSI Debt as Indebtedness. A450. As noted earlier, Save Mart's audited financial statements (2018-2020, attached to the EPA) identify SSI as an asset line item (Investment in Joint Venture) at net carrying value only. A1255, A1260, A1269-A1270. Specific SSI assets and liabilities, including SSI Debt, are not itemized in the Save Mart balance sheet. A1255, A1260, A1269-A1270.

9. <u>Closing</u>

On March 21, 2022, Seller presented the initial draft Pre-Closing Statement, under section 1.4(a), which did not list SSI Debt as part of Indebtedness. A2632-A2633 (email), A2634 (spreadsheet). By March 25, Buyer had assumed control of the document and circulated the agreed-upon final form of the Funds Flow, including again the Determination of Estimate Purchase Price, which also did not list SSI Debt

as Closing Date Indebtedness. A1881-A1886. On March 28, the transaction closed with Seller receiving a net payment of $32,590,731.29 and a further $7 million Seller's escrow (funded by Buyer). A1886 (Final Funds Flow). With full knowledge of SSI Debt and that it had not been included in Closing Date Indebtedness, Buyer closed.

10. <u>Buyer's Post-Closing Adjustment</u>

On June 27, 2022, after Closing, as provided in section 1.4(d) of the EPA, Buyer returned its Closing Statement to Seller, asserting the full SSI Debt as Indebtedness. A817-A827. To add insult to injury, Buyer did not adjust this figure to a pro rata amount reflecting that it had acquired only a fractional interest in SSI (since SSI is a general partnership), nor did it offset for the substantial SSI inventory or accounts receivable (the fruits of that debt and the assets available to satisfy that debt). A821. Thus, through a single post-Closing accounting change, Buyer purported to unilaterally shift $109,809,477.86—more than 40% of the entire purchase price—from Seller to Buyer. A821. This also amounted to a full inversion of the SSI Purchase Price: instead of Buyer paying Seller $90 million, *Seller* was now paying *Buyer* a net of more than $19 million for taking over Seller's valuable interest in SSI. A821. As the Court of Chancery noted, Buyer had "radically changed the economics in its favor" in a way that simply "made no sense." Ex. A, 4-5.

B. PROCEDURAL HISTORY

1. The Arbitration

Seller promptly disputed this radical accounting deviation, and the parties agreed to arbitrate it. A506-A511, A828-A834. All conventional disputes regarding Buyer's other proposed adjustments to the purchase price (totaling about $29.3 million) were submitted to an accounting referee. *See* A506-A511, A1051-A1078.

Following the arbitration process, the Arbitrator issued an Award in Petitioners' favor. A312-A364. The Arbitrator found dispositive the EPA's definition of Closing Date Indebtedness ("the aggregate amount of all Indebtedness of the Group Companies as of the Adjustment Time, as may be adjusted pursuant to Section 1.4"), concluding SSI Debt could fit within that definition and should therefore be used to adjust the purchase price. A325. The Arbitrator determined the Accounting Rules, generally, were *not applicable at all* to the construction of Indebtedness. A334-A346.

To justify this construction, the Arbitrator noted the *first reference* to Accounting Rules in section 1.4(d) provides they apply only "as applicable." A337-A342. Because only the definition of Working Capital re-refers to the Accounting Rules (while other definitions such as Closing Date Indebtedness do not), the Arbitrator decided the Accounting Rules only constrain Working Capital, and nothing else. A337.

Seller proposed that the phrase "as applicable" meant only that, as to any asset or liability, specific parts of the Accounting Rules might or might not apply. A286. Seller noted that section 1.4(d) referred to the Accounting Rules *twice*. A374. The second time, the phrase "as applicable" *does not appear at all*; instead, the second reference says directly that Buyer shall not adopt a construction or classification of the adjustable components, including Closing Date Indebtedness, that is "different than the Accounting Rules." A374.

When asked to identify any documentary evidence that, before Closing, Buyer believed SSI Debt was includable in Indebtedness, no Buyer witness could do so. A2322, A2398, A2456, A2472. In fact, Kingswood witnesses conceded they both (a) knew at least as early as March 21, 2023, that Seller understood the EPA did not classify SSI Debt as Indebtedness and yet (b) made the "strategic" decision not to raise the SSI Debt issue pre-Closing because they thought it would be "contentious." A2167, A2403, A2468.

The Arbitrator conceded, variously, that extrinsic evidence was "at odds with" and "in tension with" the inclusion of SSI Debt as Closing Date Indebtedness (A315, A357), and mused that Buyer "struggles to explain much of this extrinsic evidence" (A315). But he declined to come to grips with any of this devastating evidence. A316. Instead, he *excluded* Seller's extrinsic evidence on the grounds that treating

SSI Debt as Closing Date Indebtedness, and not part of the fixed, aggregate SSI Purchase Price, was the *only reasonable construction*. A315.

The Arbitrator dismissed numerous references to SSI and even *the only specific reference* to SSI Debt itself in the EPA, finding that each, considered in *isolation*, was insufficient to show that Seller's proposed construction (that SSI Debt was accounted for within the SSI Purchase Price) was plausible. A330-A352. These references included:

- **EPA, § 6.14 (SSI Interest Sold Separately)**. At Buyer's request, the EPA was amended to provide the SSI interest was to be distributed out of Save Mart and sold separately for $90 million to Buyer or its designee, with the overall purchase price to be "decreased by the SSI Purchase Price." A330-A334, A432-A433.
- **EPA, § 1.2 (Determination of Estimated Purchase Price)**. As amended just before Closing, section 1.2 specified Closing Date Indebtedness and the SSI Purchase Price as distinct components of the purchase price, stating expressly the $90 million price to be paid by Buyer's designee Topco is the "aggregate consideration" for the holding company established by Seller to hold the SSI interest. A330-A334, A372.
- **EPA, § 1.4 (Purchase Price Adjustment)**. Although, as contemplated by section 6.14(b), the EPA was amended before Closing to specify Topco as the

purchaser of the SSI interest, section 1.4 (adjustments to purchase price) was not contemporaneously amended (as one might expect if Buyer's position were correct), to either: (a) allow adjustment of the aggregate $90 million SSI Purchase Price; or (b) give Topco any adjustment rights whatsoever. A334-A346, A373-A378.

- **EPA, § 3.6 (Disclosure Schedules)**. SSI Debt was specifically identified in section 3.6 of the Disclosure Schedules, the only specific reference to SSI Debt. A346-A352. Review of section 3.6 of the EPA confirms that a debt could *either* be listed in section 3.6 of the Disclosure Schedules *or* part of Indebtedness, *but not both*. A384.

Responding to Seller's claim that treatment of SSI Debt as Closing Date Indebtedness would provide a $109 million windfall to Buyer, the Arbitrator noted that, as provided in the Letter of Intent, the transaction was to be "cash free and debt free."[3] A354, A516. At the same time, the Arbitrator refused to consider the more specific portion of the Letter of Intent that provided a specific list of Indebtedness that did *not include* SSI Debt. A315, A522.

[3] Notably, this "cash free and debt free" language does not appear in the EPA, but rather is a phrase used in the parties' LOI. A516. In other words, this is *extrinsic* evidence the Arbitrator relied on while rejecting Seller's extrinsic evidence. A354.

2. The Court of Chancery's Decision

Buyer filed a petition to confirm the Award, and Seller filed an answer and counterclaim to vacate the Award. A28-A45, A246-A305. After briefing, the Court of Chancery heard argument and issued an order "reluctantly" confirming the Award. Ex. A, 1.

The Court of Chancery determined that under a "literal" reading, the definition of Closing Date Indebtedness could include SSI Debt. However, the court then explained the irrational nature of the adjustment, noting that, beyond the definition read in isolation, the adjustment had "nothing else to commend it." The court explained the adjustment flouted consistency rules and ignored that the parties had otherwise agreed on a $90 million value. The court determined Buyer's adjustment "caused the value of the Company to change based on a difference in accounting treatment," that "made no sense," and "radically changed the economics in its favor." Ex. A, 4-5.

The court also confirmed the "Seller historically carried the [SSI] interest as an equity investment, meaning that it reflected one-third of the value of [SSI], including a proportionate allocation of the [SSI] debt."[4] Ex. A, 4-5. Although the court identified the departure from historical standards, it did not analyze section

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[4] Technically, Save Mart owned just over 50% of SSI. A1269. SSI originally had three owners, which may explain the one-third reference. A1544.

1.4(d) of the EPA (governing Buyer's Closing Statement), nor did it expressly consider whether the Accounting Rules restrained the interpretation of Closing Date Indebtedness. Ex. A.

Instead, the court explained that it felt constrained by the standard of review that applies to arbitration awards, and particularly by this Court's decision in *SPX Corp. v. Garda USA, Inc.*, 94 A.3d 745 (Del. 2014). Ex. A, 7-10. The court stated that the Arbitrator had "strictly applied the literal words of the definition of Closing Date Indebtedness." Ex. A, 9. It therefore confirmed the Award, even while recognizing the "agreed-upon accounting principles … meant that Buyer's adjustment was contrary to the plain meaning of the Agreement" and acknowledging that it "would have ruled differently" than the Arbitrator. *Id.*

ARGUMENT

A. QUESTION PRESENTED

Did the Court of Chancery err in confirming an Award that subverted the transaction's economics by manifestly disregarding express contractual Accounting Rules designed to constrain Buyer's post-Closing adjustments? A1095-A1096, A1123-A1126, A1137-A1150, Ex. A.

B. STANDARD AND SCOPE OF REVIEW

This Court's review of a summary judgment ruling is *de novo*. *SPX*, 94 A.3d at 750. The Court considers "the factual record before the trial court and examine[s] anew the legal conclusions to determine whether error occurred in applying pertinent legal standards." *Brzoska v. Olson*, 668 A.2d 1355, 1360 (Del. 1995).

Judicial review of an arbitration award is limited but meaningful; it is not a mechanical rubber stamp. *Metromedia Energy, Inc. v. Enserch Energy Servs., Inc.*, 409 F.3d 574, 579 (3d Cir. 2005) ("[T]he courts are neither entitled nor encouraged simply to 'rubber stamp' the interpretations and decisions of arbitrators.") An arbitrator "may not shield an 'outlandish disposition of a grievance' from judicial review 'simply by making the right noises—noises of contract interpretation.'" *Leed Architectural Products, Inc. v. United Steelworkers, Local 6674*, 916 F.2d 63, 65 (2d Cir. 1990). Otherwise, parties unwilling to accept unreviewable results that

disregard even the plainest contract terms would be encouraged to forgo the unpredictable vicissitudes of arbitration in favor of more certain litigation.[5]

To facilitate the required careful judicial review of arbitration awards, Delaware courts have therefore interpreted section 10(a)(4) of the FAA to authorize vacatur "where the arbitrator acts in 'manifest disregard' of the law." *SPX*, 94 A.3d at 750 (discussing 9 U.S.C. § 10(a)(4)). Put another way, if the record is such that no reasonable arbitrator would have issued the award, it should be vacated. *Cf. Fraternal Ord. of Police, Lodge 5 v. New Castle Cnty.*, 2014 WL 351009, at *10 (Del. Ch. Jan. 29, 2014) (denying vacatur "[b]ecause a reasonable arbitrator could have found" the evidence supported the underlying award). That level of unreasonableness is present where "the arbitrator was 'fully aware of the existence of a clearly defined governing legal principle but refused to apply it, in effect, ignoring it.'" *SPX*, 94 A.3d at 750 (quoting *Duferco Int'l Steel Trading v. T. Klaveness Shipping A/S*, 333 F.3d 383, 389 (2d Cir. 2003)). It can be shown "where a governing legal principle is 'well defined, explicit, and clearly applicable to the case,' and where the arbitrator ignored it after it was brought to the arbitrator's attention in a way that assures that the arbitrator knew its controlling nature." *Goldman v. Architectural Iron Co.*, 306 F.3d 1214, 1216 (2d Cir. 2002).

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[5] Parties cannot address this issue themselves. *Hall St. Assocs., L.L.C. v. Mattel, Inc.*, 552 U.S. 576, 588 (2008) (holding that parties cannot contract for greater judicial review of arbitration awards than the FAA allows).

This standard can be met in a contract case if "the arbitrator consciously chose to ignore a legal principle, *or contract term*, that is so clear that it is not subject to reasonable debate." *Stempien v. Marnie Properties, LLC*, 2017 WL 6016568, at *1 (Del. Ch. Nov. 3, 2017) (emphasis added) (denying motion to dismiss a petition for vacatur because the plaintiffs sufficiently alleged the arbitrator "acted with a manifest disregard of the law by awarding fees and expenses to Defendant that were plainly not allowed under the contract").

When an arbitrator acts in manifest disregard of the law, upholding the arbitrator's decision becomes "contrary to the same public policy which animates the courts' deference toward arbitration." *Travelers Ins. Co. v. Nationwide Mut. Ins. Co.*, 886 A.2d 46, 47 (Del. Ch. 2005). Under such circumstances, the arbitration award must be vacated, and "[a]ny other result would be a gross injustice." *Id.* On application of these standards here, the Award is properly vacated.

C. MERITS OF ARGUMENT

1. The Arbitrator Manifestly Disregarded the Law by Disregarding the Accounting Rules, which Prohibited Both Double Counting and Accounting Inconsistent with Save Mart's Historical Practices

The Award subverted the deal economics by disregarding express textual constraints intended to prevent that outcome and the post-Closing gamesmanship that led to it. Under section 1.4(d) of the EPA, Buyer's ability to adjust the purchase price after Closing was expressly constrained by the Accounting Rules:

> *The Closing Statement shall be prepared in a manner consistent with the definitions of the terms Working Capital, Closing Cash, Closing Date Indebtedness, Transaction Expenses, including, as applicable, the Accounting Rules (including as reflected on Exhibit A).* **The Parties agree that the purpose of preparing the Closing Statement and determining the Working Capital, Closing Cash, Closing Date Indebtedness, and Transaction Expenses is to measure the amount of the Working Capital, Closing Cash, Closing Date Indebtedness, and Transaction Expenses and such processes are not intended to (x) permit the introduction of accounting methods, policies, principles, practices, procedures, classifications or estimation methodologies for the purpose of determining the Working Capital, Closing Cash, Closing Date Indebtedness, or Transaction Expenses that are different than the Accounting Rules** … .

A374 (emphasis added). *Twice* this provision provides the Closing Statement, including Indebtedness and the other adjustable components, is constrained by the Accounting Rules. A374. Yet, the Arbitrator refused to apply this crucial restraint, and in confirming the Award, the Court of Chancery also overlooked that the Accounting Rules constrain the definitions. A334-A346.

The Arbitrator took the first reference to the Accounting Rules in section 1.4(d) (*italicized* above), and specifically the qualifier "as applicable," as license to disregard the Accounting Rules altogether when calculating Indebtedness (or any of the other adjustable components of the purchase price, except for Working Capital). A337. The Arbitrator thereby separated the definition of Indebtedness from the broader context of the EPA.[6] *Cf. OSI Systems, Inc. v. Instrumentarium Corp.*, 892

[6] In accepting Buyer's allocation of SSI Debt to Indebtedness, instead of including it as part of the fixed, aggregate, and more *specific* SSI Purchase Price, the Arbitrator

A.2d 1086, 1092 (Del. Ch. 2006) (clarifying and rejecting "isolated reading" of one section in light of review of the purchase agreement, generally); *In re IAC/Interactive Corp.*, 948 A.2d 471, 507 (Del. Ch. 2008) (rejecting construction of durable proxy dependent on narrow construction of one provision after review of broader agreement). The Arbitrator thus disregarded Delaware law, which requires a cohesive interpretation that harmonizes and gives effect to the entire agreement and the parties' intended transaction. *Osborn v. Kemp*, 991 A.2d 1153, 1159-60 (Del. 2010).

If the intent were to make the Accounting Rules applicable only to Working Capital, the sentence would have been written differently (*e.g.*, "Working Capital (subject to the Accounting Rules), Closing Cash, Closing Date Indebtedness, and Transaction Expenses"). Instead, the "as applicable" phrase appears at the end of this sentence describing how the Closing Statement will be prepared, and it is separated from "Working Capital" by three other components—including Indebtedness. A374. The phrase "as applicable" thus simply makes clear that specific components of the Accounting Rules (*i.e.*, any one Agreed Principle or

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also prioritized a general construction over a more specific one, contrary to a critical canon of construction. *DCV Holdings, Inc. v. ConAgra, Inc.*, 889 A.2d 954, 961 (Del. 2005) ("[W]here specific and general provisions conflict, the specific provision ordinarily qualifies the meaning of the general one.").

Historical Principle) may (or may not) apply to specific assets or liability items within the Closing Statement. Any other reading is unreasonable.

Review of the Accounting Rules themselves confirms the EPA did not permit the Arbitrator to cast them aside when calculating any adjustable component of the Purchase Price. For instance, the Agreed Principles in Exhibit A to the EPA, specified as the first Accounting Rule, include the following general references to the Statements (and not just the Working Capital component thereof) along with some specific references to Working Capital:

> This exhibit sets forth details of the **Agreed Principles that will be taken into account in determining the Pre-Closing Statement and the Closing Statement (the "Statements")**.
>
> * * * *
>
> 1. **The Statements** shall be prepared on the basis that the Group Companies are a going concern … .
>
> 2. **The Statements** shall be based on facts and circumstances as they exist as of the Adjustment Time … .
>
> 3. The provisions of this Exhibit A shall be interpreted so as to avoid double counting (whether positive or negative) **of any item to be included in the Statements**.
>
> 4. Working Capital shall include only those specific accounts and line items set forth in Part II … .
>
> 5. Except for the physical inventory count procedures, Working Capital shall include inventory prepared as if the Adjustment Time occurs at a fiscal year-end … .

A472-A473 (emphasis added). Some of the Agreed Principles are specific to Working Capital alone, while other sections, including the introduction, refer to the

Statements generally. A472-A473. For example, the rule against double counting (in Principle 3) applies to "any item to be included in the Statements," which of course includes Indebtedness. A472-A473. No reasonable arbitrator could read the EPA to apply these Agreed Principles only to Working Capital and otherwise disregard them.

Even if there were doubt as to the proper construction of the first reference to the Accounting Rules in section 1.4(d) (including the "as applicable" phrase), the second reference to Accounting Rules in section 1.4(d) (**bold** above) dispels that doubt. The second reference confirms the Accounting Rules apply to each adjustable component of the purchase price, not just Working Capital. A374. In the second reference, the parties agreed the post-Closing adjustment process was "not intended to … permit the introduction of accounting methods … [or] classifications … for the purpose of determining Working Capital, Closing Cash, Closing Date Indebtedness, and Transaction Expenses that are different than the Accounting Rules." A374. The "as applicable" qualifier, on which the Arbitrator relied for jettisoning the Accounting Rules as to Indebtedness (A337), is not used here. A374. This second reference unequivocally states the Accounting Rules apply to all adjustable components. When read together with the first reference and the Agreed Principles, the conclusion is inescapable: the Accounting Rules properly constrain each adjustable component of the Purchase Price. In refusing to apply the

Accounting Rules to Indebtedness, the Award manifestly disregarded the EPA, eviscerating Seller's primary protection against wild, post-closing swings and generating an outcome profoundly inconsistent with the parties' intent.

Particularly instructive is the Third Circuit's decision in *Monongahela Valley Hospital Incorporated v. United Steel Paper & Forestry Rubber Manufacturing Allied Industrial & Service Workers International Union AFL-CIO CLC*, 946 F.3d 195, 199 (3d Cir. 2019). There, the Third Circuit affirmed the district court's decision to vacate an arbitration award for manifest disregard because "an arbitrator 'may not ignore the plain language of the contract.'" *Id.* at 199. The contract at issue was a collective bargaining agreement ("CBA") between a hospital and its employee union. The CBA stated that "[v]acation will, **so far as possible**, be granted at times most desired by employees," but the hospital also had "final" and "exclusive" right to deny employees their desired vacation times and the authority to "unilaterally" change a vacation schedule. *Id.* at 197-200 (original emphasis).

Despite that contract language, the arbitrator's award found that, "'notwithstanding the Hospital's reservation of exclusive rights contained in [the CBA],' the CBA precluded the Hospital from using 'blackout' periods and prevented it from 'deny[ing] senior employees in the bargaining unit their desired vacation[ ] when there is no operating need.'" *Id.* at 198 (original brackets). It was the arbitrator's view that "the 'so far as possible' language must be given some meaning

lest the rights of the bargaining unit employees with respect to vacations 'could always be negated.'" *Id.* at 200.

On review, the Third Circuit had no trouble affirming the district court's decision rejecting the arbitrator's interpretation. Focusing on the language of the contract, the court reasoned that the phrase "'[s]o far as possible' cannot hold hostage what follows here. It is a subordinate phrase clearly qualified by the superseding 'but,' and what follows grants the Hospital the 'final,' 'exclusive[ ]' and 'unilateral[ ]' right to schedule vacations." *Id.* (original brackets). As the court further explained, the arbitrator could not reasonably read that language in isolation because, when "*[p]ut in context*, 'so far as possible' means the Hospital should consider in good faith the bargaining unit employees' preferences when exercising its final and exclusive right to determine vacation, but nothing more; and there is certainly no requirement anywhere in the CBA that the Hospital consider operating need." *Id.* (emphasis added). Thus, even though it acknowledged that it was duty bound to apply a "a standard of review tilted much in favor of arbitrators," the Third Circuit held that it "cannot affirm this award that manifestly disregards the plain language of the CBA." *Id.*

The conflict between the Award and the contract in this case is more pronounced than the departure from the contract language that the *Monongahela* court held constituted a manifest disregard of the law. In *Monongahela*, the

arbitrator could at least hang his hat on express language ("so far as possible") as a constraint on what otherwise appeared to be an intent to vest ultimate power in the hospital to assign schedules. *Id.* at 198. Yet, the district court and Third Circuit both held that such general language could not override the express, repeated reservation of ultimate authority to the hospital, especially when that language was read in context. *Id.* at 200. Here, however, the Arbitrator's isolated emphasis on "as applicable" radically rewrites the EPA to eviscerate the express terms and clear intent of the Accounting Rules. If simply holding express terms "hostage" by reading parts of the contract in isolation constitutes a manifest disregard of the law (as in *Monongahela*), disregarding terms as the Arbitrator did here surely is too.

Worse still, the Arbitrator's interpretation here violated the Accounting Rules' prohibitions on (a) double counting of any item (A472); and (b) the use of accounting principles or classifications (*i.e.*, the proper classification of SSI Debt) that differ from those used in preparing the Company Financial Statements dated December 27, 2020 (the "Historical Principles") (A450). If these Accounting Rules apply to the determination of Closing Date Indebtedness, there is no logical way to include SSI Debt in that category.

There can be no doubt that including SSI Debt in Closing Date Indebtedness constitutes double counting because, as confirmed by the Court of Chancery, SSI Debt was fully accounted for in the SSI Purchase Price. Ex. A, 4-5. This is also

confirmed by the fact that SSI Debt was specifically identified in section 3.6 of the Disclosure Schedule and so cannot properly surface in the alternative adjustable categories, such as Closing Date Indebtedness. A1799. Moreover, because Save Mart never counted SSI Debt as its own long term debt, it cannot, consistent with Historical Principles, be counted as long term debt by Buyer in its post-Closing adjustment.[7] In at least two distinct ways, inclusion of SSI Debt within Indebtedness violates the Accounting Rules and therefore is not permissible. The Arbitrator acted beyond his authority by disregarding the Accounting Rules and adopting an interpretation that flagrantly flouts their express purpose.

2. **The Arbitrator Improperly Selectively Relied on Extrinsic Evidence Supporting Buyer's Position While Disregarding Such Evidence Supporting Seller's Position**

In addition to disregarding provisions of the EPA, the Arbitrator improperly picked and chose among the extrinsic evidence he was willing to consider. He based his interpretation on the notion the parties intended "a cash free and debt free transaction." A354. Yet, despite his insistence that such language appeared "on its face" in the EPA, it actually appears nowhere in the contract. *See* A365-A500. Instead, the phrase "cash free and debt free" comes from *extrinsic evidence* (the

[7] The Award suggests this argument was "largely absent from [Seller's] post-hearing submissions." A345. Not so. A1004, A1010-A1014 (extensive briefing on how Accounting Rules, including Historical Principles, preclude treatment of SSI Debt as Indebtedness).

LOI). A516. But while the Arbitrator relied on that evidence, which supposedly supported his interpretation, at the same time he refused to consider the mountain of devastating extrinsic evidence showing that Buyer never believed it was entitled to recover SSI Debt as Indebtedness and the SSI Purchase Price had been determined net of SSI Debt. A314-A315. Critically, as explained above, Buyer's own accountants reviewing the transaction unequivocally stated that SSI Debt would "not be includable in Indebtedness" because it was outside the consolidation perimeter of Save Mart (meaning that SSI was not entirely consolidated into Save Mart, but rather treated only as a net asset). A1755. There is no evidence of any contemporaneous disagreement by Buyer with that straightforward—and correct—assessment.

The Arbitrator justified his refusal to consider Seller's extrinsic evidence by explaining that "when faced with tension between unambiguous contract terms supporting one result and extrinsic evidence supporting another, Delaware courts have consistently and reliably resolved the dispute based on the contract's plain language." A357. The Arbitrator did not, however, cite any court, in Delaware or elsewhere, that permits selective consideration of extrinsic evidence supporting one interpretation while barring material extrinsic evidence offered in support of another, far more logical interpretation—especially evidence that, as the Arbitrator conceded, "appear[ed] to be at odds with" his reading of the EPA. A357; *cf. Eagle Indus., Inc. v. DeVilbiss Health Care, Inc.*, 702 A.2d 1228, 1233 (Del. 1997) (concluding trial

court should have considered extrinsic evidence and instructing court on remand to "consider *any admissible* extrinsic evidence that may shed light on the expectations of the parties at the time they entered into the Agreement." (emphasis added)).

The obvious problem inherent in relying on extrinsic evidence supportive of only one contract reading is especially palpable here because the Accounting Referee overseeing the parallel dispute involving more conventional Buyer adjustments (such as material payments to the CEO for severance) had no trouble rejecting Buyer's interpretation without the benefit of *any* extrinsic evidence. A1074-A1075. The Referee disagreed with Buyer's contention that, under section 1.4(d), another adjustable component (Transaction Expenses) should be determined without reference to the Accounting Rules. A1074-A1075. Citing the first reference to the Accounting Rules in section 1.4(d) (including the "as applicable" phrase), the Referee held the *entire Closing Statement*, including Transaction Expenses, was to be prepared consistent with the Accounting Rules. A1075. By contrast, the Arbitrator acted unreasonably by selectively relying on extrinsic evidence to adopt an interpretation that disregarded the express Accounting Rules.

3. Post-Closing Adjustments Are Not Occasions for Ambushing Counterparties with New Accounting Classifications that Profoundly Change Deal Economics

The Arbitrator's refusal to apply the Accounting Rules as a limit on the determination of Indebtedness under section 1.4(d) is particularly problematic given

well-established case law rejecting post-closing adjustments, like this, contrary to a company's historic accounting methods. *See OSI*, 892 A.2d at 1091 (rejecting $30 million reduction in working capital (out of an original $84 million) on grounds that adjustment modified underlying accounting principles); *Westmoreland Coal Co. v. Entech, Inc.*, 100 N.Y.2d 352 (2003) (rejecting $74 million reduction to $138 million purchase price on grounds that buyer attempted to vary accounting methods); *Chicago Bridge & Iron Co. N.V. v. Westinghouse Elec. Co. LLC*, 166 A.3d 912, 923-24 (Del. 2017) (calling into serious question buyer's post-closing "challenges to large [and known] items included in the financial statements"). Under Delaware law, any such adjustments must maintain "the underlying economics of the parties' bargain." *Chicago Bridge*, 166 A.3d at 930. And yet, as the Court of Chancery recognized, Buyer's cynical adjustment instead "radically changed the economics in its favor."

That most certainly is not what purchase price adjustments are for. To the contrary, they serve the limited purpose of "account[ing] for the normal variation in business from signing until closing to assure the buyer and seller that the purchase price accurately reflects the target's financial condition at the time of closing." *Id.* at 928; *see also Avnet, Inc. v. H.I.G. Source, Inc.*, 2010 WL 3787581, at *1 (Del. Ch. Sept. 29, 2010) ("Parties typically adopt such procedures because, among other reasons, some of the merger consideration components, e.g., working capital, are

constantly changing and, therefore, need to be estimated for purposes of the closing, subject to later adjustment."). But here, Buyer's adjustment stemmed not from some modest pre-Closing variation in the business, but rather from a radical recharacterization of longstanding SSI Debt that had been separately specified in section 3.6 of the Disclosure Schedule.

In *Chicago Bridge*, this Court specifically criticized buyer Westinghouse's effort to use the post-closing price adjustment process to challenge "large items" that "Westinghouse knew about before closing" yet did not use as a basis not to close, noting that "Westinghouse now says that it should keep [seller's former subsidiary], which it got for zero dollars, and be paid by Chicago Bridge over $2 billion for taking it!" *Chicago Bridge*, 166 A.3d at 924. *Chicago Bridge* is not an isolated decision, but follows *Westmoreland*, 100 N.Y.2d at 358-59, and *OSI*, 892 A.2d at 1091—both cases where large post-Closing adjustments inconsistent with historical financials were rejected. The same principles apply here.

There can be no doubt that affirming the judgment and Award here would work a gross injustice. Buyer was well aware of SSI Debt, was not concerned about it, did not assert it pre-Closing, and instead "strategically" waited until post-Closing to try to secure a $109 million windfall. A1168-A1169, A2167, A2403, A2468. Although Buyer had agreed to pay a fixed, aggregate price of $90 million for the SSI interest, the SSI Debt adjustment *fully reverses* the flow of consideration for the SSI

interest so that instead of receiving $90 million for this valuable asset, Seller is paying Buyer more than $19 million for taking Seller's asset. A821. The caselaw makes clear, and this Court should take this opportunity to confirm, that kind of behavior cannot be rewarded. *Cf. In re IAC/Interactive Corp.*, 948 A.2d at 501 (firmly rejecting proffered interpretation where party could not point to any contemporaneous, extrinsic writing supporting its position). Preventing this very kind of cynical gamesmanship is at the heart of cases such as *Chicago Bridge*, *OSI*, and *Westmoreland*; yet here, the Award, as confirmed by the Court of Chancery, endorses Buyer's brazen gambit.

4. **The Court of Chancery—Even While Acknowledging the Award Made No Sense—Deferred to the Arbitrator Without Addressing the Accounting Rule Constraints**

The Court of Chancery acknowledged the Arbitrator's Award totally subverted the deal economics—making Seller pay for what Buyer "bought"—but nevertheless confirmed the Award. Ex. A, 4-5. In reaching this decision, the court relied heavily upon its own experience in *SPX Corp. v. Garda USA, Inc.*, 94 A.3d 745, 750 (Del. 2014), where this Court reversed the same Vice Chancellor's order vacating an arbitration award. It is understandable that a trial court once bitten may be twice shy. However, contrary to the court's analysis below, *SPX* is not dispositive here. In *SPX*, the question presented was whether the following provision

unambiguously required inclusion of "incurred but not reported" workers compensation liabilities:

> a) The calculation of current assets and liabilities shall exclude the following accounts and balances:
>
> * * *
>
> v. Incurred but not reported and reported claims related to risk management programs, with the exception of those workers' compensation liabilities, which shall be included in the calculation of current liabilities;

Ernst & Young, acting as Referee, determined this language would not require the inclusion of "incurred but not reported" workers' compensation claims; but, rather, the seller's inclusion of only reported claims under the company's longstanding practice was sufficient. The dispute was whether the exception for workers compensation claims was intended to apply to both "incurred but not reported" AND "reported" claims, or just the reported claims. The answer to this question was far from clear, especially where the company had never before estimated "incurred but not reported" workers' compensation claims.[8] This Court reversed the trial court's decision to vacate the award, noting that "there were two colorable interpretations," and therefore there was no apparent manifest disregard of the contract.

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[8] In fact, for this reason, Ernst & Young's decision is the least surprising result. The purpose of the post-Closing process is to identify changes occurring around Closing and to avoid surprise, not to allow a buyer to modify, or even inject new, accounting methods into a transaction after Closing. E&Y's decision was consonant with past practice, while buyer's advocacy to include "incurred but not reported" claims would have been a departure from historical practice.

By contrast, in the instant case, there is no plausible interpretation of section 1.4(d) (the section addressing Buyer's Closing Statement) that would allow an arbitrator to ignore the Accounting Rules and reclassify SSI Debt as Indebtedness—a classification directly at odds with the rule against double counting and the Historical Principles. In the court's order, however, there is no discussion of the import of section 1.4(d). Ex. A. Instead, as in the Award, the focus is on the definition of Indebtedness. *Id.* This isolated analysis is incomplete and, as discussed above, is out of step with *Monongahela*, *OSI*, and *IAC/Interactive*. On a proper application of Delaware law, there is no plausible way in which section 1.4(d) can be read to isolate the definition of Indebtedness from the plain, express, repeated, crucial, and common constraints of the Accounting Rules.

The Award manifestly disregards the express terms of the EPA, well-established legal principles, and governing case law. It thereby generates a grossly unjust and indefensible result—one that if affirmed will deter use of arbitration generally. For these reasons, the order confirming the Award should be set aside.

CONCLUSION

For the foregoing reasons, Seller respectfully requests that the Court reverse the judgment of the Court of Chancery and instruct it to vacate the Award.

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Dated: May 7, 2024

CERTIFICATE OF SERVICE

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